



THE CITY OF SAN DIEGO MANAGER'S REPORT

DATE ISSUED: March 18, 2002 **REPORT NO.** 02-061

ATTENTION: The Committee on Rules, Finance and Intergovernmental Relations
Agenda of March 20, 2002

SUBJECT: Response to the Blue Ribbon Committee Report

REFERENCE: Blue Ribbon Committee Report on City of San Diego Finances - February 2002

SUMMARY

Issue: Should the City of San Diego implement the Blue Ribbon Committee's recommendations for the City's continued fiscal health?

Manager's Recommendations: Analyze the Blue Ribbon Committee's recommendations and return to the City Council with proposed implementation strategies.

Other Recommendations: None

Fiscal Impact: Several of the Blue Ribbon Committee's recommendations will require additional funding that will need to be identified in conjunction with the development of solutions to the issues raised by the Committee.

BACKGROUND

In April 2001, the Mayor convened the Blue Ribbon Committee on City Finances to perform an independent evaluation on the City's current fiscal health and make appropriate recommendations. The objectives of the Committee were to perform an independent evaluation of the fiscal health of the City of San Diego, review the budgeting principles of the City of San Diego, and report findings and recommendations to Mayor Dick Murphy.

Overall, the Committee found that the City is fiscally sound. However, it identified several areas of concern which could potentially have an impact on the fiscal health of the City in future years. The areas of concern included General Reserves and Insurance, Retirement Benefits and

Unfunded Pension Liabilities, General Deferred Maintenance and Unfunded Procurement, Revenues and Expenditures, and Principles of Budgeting and Finance.

The City Manager agrees with the Committee's recommendations and consistent with the Blue Ribbon Committee's suggestion, will return with a progress report to the Rules Committee in March 2003. Prioritization of each recommendation will be based on the impact to the General Fund, availability of resources, time for completion, and the opportunity to improve the City's fiscal health.

DISCUSSION

The Blue Ribbon Committee Report made ten recommendations to improve the fiscal health of the City of San Diego. The Blue Ribbon Committee Report is attached. This City Manager's Report is in response to the Blue Ribbon Committee Report and lists each Blue Ribbon Committee recommendation and the methods the City Manager proposes to implement these recommendations.

General Reserves and Insurance

Blue Ribbon Recommendation #1: Evaluate and determine what an adequate reserve level is for the City. The Committee recommends increasing the reserves to be between 7-10% of General Fund Revenues.

It is understood that San Diego must have sufficient funds in reserve that are available in a time of fiscal crisis to cover unplanned short-term economic downturns or address emergency situations. The City's General Reserves have more than doubled since 1997 and are currently \$30.5 million (approximately 4% of the Fiscal Year 2002 General Fund revenues). The City Manager will evaluate the current reserves and develop recommendations. The City Manager agrees that total General Reserves should be monitored to ensure that a sufficient reserve is maintained.

Retirement Benefits and Unfunded Pension Liabilities

Blue Ribbon Recommendation #2: Change the City's Funding strategy to one that results in the City fully funding its future obligations earned today which includes the pension benefits as well as health benefits.

Blue Ribbon Recommendation #3: Obtain a current and comprehensive analysis of projected pension expenses and revenue sources, which includes the current present value of retiree health benefits to determine the impact on future City finances.

The City Manager agrees that unfunded retiree health benefits will continue to be a liability against future revenues. The City Manager will ask the City Retirement Officer to assist the City in obtaining a comprehensive analysis of the Blue Ribbon Committee's recommendations. Upon completion of the analysis, the City Retirement Officer and the City Manager will present to the Mayor and City Council the results of the analysis and recommendations where appropriate.

General Deferred Maintenance and Unfunded Procurement

Blue Ribbon Recommendation #4: The City Manager should establish a process so that all deferred maintenance and unfunded procurement information is developed, aggregated, consistent, complete, non-duplicative, rated for priority, and is available on call for budgetary decisions.

Blue Ribbon Recommendation #5: The City Manager should prepare and present a public report during the annual budget hearings identifying the cumulative deferred maintenance backlog and unfunded procurement needs which includes asset descriptions, dollar requirements, and categorized by level of need with funding sources.

The City Manager concurs that physical assets require periodic major maintenance and that a comprehensive inventory would assist in prioritizing projects. In order to assess the magnitude of maintaining and/or replacing major capital items, the City Manager will explore opportunities to develop a consistent and non-duplicative ongoing assessment of all City assets so that information will be available annually during budget hearings. Although these efforts will be initiated at this time, the development of a comprehensive list may not be available in time for the Fiscal Year 2003 budget hearings.

During the past year, the General Services Department has addressed two important aspects of the issues raised by the Committee. First, the City's non-public safety fleet was evaluated relative to size and condition. As a result, the fleet was downsized by approximately 150 vehicles thus saving \$1 million annually, and the acquisition program was restructured utilizing lease-purchases to insure timely replacement of fleet vehicles. This restructuring resulted in a one-time savings of \$2 million, which will be returned to the General Fund in Fiscal Year 2003.

Secondly, an assessment of the City's buildings was undertaken approximately eight months ago. This assessment will update the 1990 study evaluating the condition of the City facilities and placing a value on the deferred maintenance of those facilities. In addition to the update of the earlier report it will provide a guide in developing a consistent and accurate ongoing assessment of all City facilities.

Blue Ribbon Recommendation #6: The City's policy with respect to funding deferred maintenance and Information Technology procurement should be revised to increase expenditures in these crucial areas. While the Committee notes some improvement in addressing deferred maintenance needs in some specific areas, other areas continue to deteriorate.

The Committee believes that the City's backlog of general deferred maintenance exceeds \$300 million. In addition, the City estimates \$120 - \$170 million in Information Technology needs over the next five years. The City Manager will make funding recommendations in the annual budget process based upon the deferred maintenance assessments, unfunded procurement priorities, availability of revenues and overall budget priorities.

Revenues and Expenditures

Blue Ribbon Recommendation #7: Expand the current revenue sources and seek additional sources of revenue.

In comparison to other large cities in California and the nation, the City has a relatively low revenue base. Despite efforts during recent years to incorporate new General Fund revenue

options into the City's budget, such as the Corporate Sponsorship Program, which was instituted in Fiscal Year 2000, San Diego has assessed few new fees and has adopted no additional tax increases to existing General Fund revenues. The only significant new fees or revenue increases were the implementation of the Refuse Collector Business License Tax, and the increase in the Transient Occupancy Tax rate from 9 percent to 10.5 percent, which were adopted during the 1990s. In addition, the City has actually reduced some fees in an effort to become more business-friendly.

The City of San Diego does not collect revenue for refuse collection and utility user taxes. In addition to the City's low revenue base, for fiscal years 1991-2002 the State of California diverted approximately \$283 million of revenue away from the City of San Diego. This diversion has lowered the City's revenue base thus contributing to the deferred maintenance issue. In 1990, two of the major General Fund revenue sources, Property Tax and Sales Tax, were sufficient to fund the entire public safety budget; however, today these revenue sources cover only 80 percent of public safety allocations. Additional revenue could help fund general City operations, public safety, deferred maintenance, information and technology, and the Strategic Framework Element of the General Plan Update including the City of Villages concept.

In light of the current recession, the City of San Diego may want to consider revenue-generating options, which may include new assessments such as a Refuse Collection Fee and Utility User Tax and increases to existing revenue sources such as the Storm Drain Fee, Property Transfer Tax, Transient Occupancy Tax, and Sales Tax. The City Manager will work with the Mayor, City Council and key stakeholders to explore options for expanding the City's revenue base.

Blue Ribbon Recommendation #8: Seek ways to reduce expenditures through improved operational efficiencies or elimination of specific services in deference to higher priority needs.

The City has reduced expenditures and improved operational efficiencies by implementing its Performance Management Program and establishing the Select Committee on Government Efficiency & Fiscal Reform (Select Committee). The key elements of the Performance Management Program include Performance-Based Budgeting, the Optimization Program, Zero-Based Management Reviews (ZBMR), Performance Audits and benchmarking. Since 1994, the ZBMR and Optimization Program have served to stimulate numerous process improvements, cost reduction initiatives, and has saved the City over \$100 million. The Select Committee also charged with initiating change efforts and finding innovative solutions for streamlining and downsizing city government, has been effective in implementing recommendations from the Mayor's Task Force, the City Council, and other committees.

In addition, the City Manager for fiscal years 2002 and 2003 requested that General Fund departments take a critical look at their operations and achieve at least a 2% expenditure savings. The City Manager will continue to review expenditures and pursue opportunities to improve operational efficiencies with the support of the above ongoing programs. Additionally, all City of San Diego services will be reviewed by the City Manager to identify funding priorities in light of limited revenue sources.

Principles of Budgeting and Finance

Blue Ribbon Recommendation #9: The City should follow its existing six budget principles and add two additional budget principles:

Proposed Principle #7: Budget development should be guided by a long term, or

strategic budget plan proposed by the Manager and adopted by the Council.

Proposed Principle #8: Once adopted, annual budgets should be amended only when urgency requires, and then by identifying specific funding sources for these new priorities.

The City Manager will add these principles and incorporate them into future budget development and administration.

Follow-up Issues

Blue Ribbon Recommendation #10: Submit a report in March of 2003 addressed to the Blue Ribbon Committee on Finances summarizing the progress on each recommendation contained in [the] report.

Consistent with the Blue Ribbon Committee's recommendation, a comprehensive report will be presented to the Rules Committee in March 2003, which will provide the status of the implementation of the Blue Ribbon Committee's recommendations.

CONCLUSION

I would like to take this opportunity to thank the members of the Blue Ribbon Committee for their objective analysis and recommendations to ensure the City's continued fiscal strength. I agree in general with the recommendations and anticipate working with the Mayor, City Council and key stakeholders in consideration of implementing the recommendations as provided by the Blue Ribbon Committee.

Respectfully submitted,

Michael T. Uberuaga
City Manager

IRVINE/CMC

Note: The attachment is not available in electronic format. Copies of the attachment are available for review in the Office of the City Clerk.

Attachment A – Blue Ribbon Committee Report on City of San Diego Finances – February 2002